MINUTES
of the
FOURTH MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

September 29-30, 2014
Golf Course Clubhouse, New Mexico State University
3000 Herb Wimberly Drive
Las Cruces

The fourth meeting in 2014 of the Revenue Stabilization and Tax Policy Committee (RSTP) was called to order by Representative Edward C. Sandoval, chair, on Monday, September 29, 2014, at 10:15 a.m. at the Golf Course Clubhouse of New Mexico State University (NMSU) in Las Cruces.

Present
Rep. Edward C. Sandoval, Chair
Sen. Carlos R. Cisneros, Vice Chair
Rep. Anna M. Crook
Rep. Rodolpho "Rudy" S. Martinez
Sen. Clemente Sanchez (9/29)
Sen. John Arthur Smith
Rep. James R.J. Strickler (9/29)
Rep. Thomas C. Taylor
Rep. Jim R. Trujillo

Absent
Sen. Sue Wilson Beffort
Rep. Brian F. Egolf, Jr.
Sen. Timothy M. Keller
Sen. Mark Moores
Rep. Henry Kiki Saavedra
Sen. William E. Sharer
Sen. Lisa A. Torraco
Sen. Peter Wirth
Rep. Bob Wooley

Designees
Sen. William F. Burt (9/29)
Sen. Jacob R. Candelaria (9/29)
Rep. Jason C. Harper (9/30)
Rep. Bill McCamley
Sen. Nancy Rodriguez (9/29)

Rep. Donald E. Bratton
Rep. Ernest H. Chavez
Rep. Miguel P. Garcia
Sen. Phil A. Griego
Rep. Sandra D. Jeff
Sen. Gay G. Kernan
Rep. Tim D. Lewis
Sen. George K. Munoz
Rep. Paul A. Pacheco
Rep. Dennis J. Roch
Rep. Debbie A. Rodella
Sen. John M. Sapien
Rep. Carl Trujillo
Rep. Luciano "Lucky" Varela
Sen. Pat Woods

Guest Legislators
Rep. Phillip M. Archuleta (9/29)
Rep. Jason C. Harper (9/29)
Rep. W. Ken Martinez (9/29)

(Attendance dates are noted for legislators who did not attend the entire meeting.)

Staff
Pam Stokes, Staff Attorney, Legislative Council Service (LCS)
Amy Chavez-Romero, Assistant Director for Drafting Services, LCS
Carolyn Peck, Intern, LCS
Tessa Ryan, Staff Attorney, LCS

Guests
The guest list is in the meeting file.

Handouts
Handouts and other written testimony are in the meeting file.

Monday, September 29

Welcoming Remarks
Dr. Garrey Carruthers, former governor of New Mexico and current president of NMSU, who was accompanied by Sharon Jones, chief of staff, NMSU, welcomed the committee to the NMSU campus and talked about several of the university's notable programmatic and capital projects, namely: turf installation at Aggie Memorial Stadium; the Burrell College of Osteopathic Medicine, a completely private enterprise, which, if accredited, will have a groundbreaking early next year; a community park with a jogging track and exercise stations; renovation of the Coca Cola weightlifting facility; construction of a spiritual center near student residences; renovation of the baseball field, which will feature covered seating; establishment of the Domenici Institute for Public Policy; construction of an undergraduate learning and study center; safety improvements to the gymnasium; Heritage Farm, an agricultural demonstration site focused on the production of cotton, chile, pecans and wine; and McFie Circle, an area near the center of campus that will feature a park. President Carruthers thanked committee members for their part in appropriating money to support the funding of several of the projects.

When solicited by a committee member for thoughts about the recent discussion surrounding tax reform and tax-based economic development, President Carruthers responded that accountability and effectiveness are key principles for improving the state of the state through the tax code. He asserted that economic development tax programs should be routinely scrutinized for effectiveness. When asked for an opinion on other matters affecting the state, President Carruthers responded that the road-funding issue is vexing but should be handled regionally, as has been done in the border region, and that existing workers' compensation laws, which he worked on and signed when he was governor and have since become model legislation for the country, should not be amended dramatically.

Revenue Forecast

Demesia Padilla, secretary of taxation and revenue, offered an update, summarized as follows, on topics of recent interest affecting the Taxation and Revenue Department (TRD).

- In the lawsuit between the City of Eunice and the TRD, the TRD petitioned the New Mexico Supreme Court for a reconsideration of its denial of *certiorari*.
- Prompted by complaints that fiscal impact reports associated with tax-related bills often inaccurately predict the fiscal effects of proposed measures, the TRD examined the situation and determined that North American Industry Classification System-code reporting is partly to blame. That is, although some companies can be classified under more than one code, they report under only one and meet the statutory requirement. The TRD is working to address the issue.
- In response to local governments' requests for better tax-related data, the TRD produces RP 500 reports, which are available online. Generally, those reports outline tax distributions to local governments. (Two samples of the report were distributed to the committee: one like those available online and one of the type not available online, which a local government may request and which provides information about particular corporate taxpayers.)
- Corporate income tax estimated payments have decreased, but compensating tax payments have grown. This trend suggests that corporate investment in equipment is on the rise, which in turn suggests that businesses are expanding.

Leila Burrows Kleats, chief economist, Department of Finance and Administration (DFA), Peter van Moorsel, chief economist, Legislative Finance Committee (LFC), and Elisa Walker-Moran, chief economist, TRD, members of the Consensus Revenue Estimating Group (CREG), updated the committee on general fund (GF) revenue history, projections and risks, commenting in particular on the U.S. economic outlook, New Mexico employment, the gross receipts and compensating tax (GRT) base, oil and gas prices, energy markets and the budget for capital projects.

Ms. Walker-Moran gave an overview of the CREG's recent work. She highlighted August 2014 revisions to the December 2013 recurring revenue estimates, all of which were increases. Those increases were largely due to current and anticipated strength in the oil and gas industries. December's estimate of fiscal year (FY) 2014 revenue was $146 million below the August estimate, and the group projects that there will be approximately $285 million of "new money" for recurring appropriations in the FY 2016 budget cycle. Ms. Walker-Moran referred to charts and tables that illustrate the steady, generally consistent increase over time in taxable gross receipts (TGRs). All sectors' TGRs have grown over the past five years, but the largest increase is associated with the oil and gas industries. Of the highest TGR-producing manufacturing subsectors, petroleum refineries are generating revenue at a level that marks the greatest recent increase.

Ms. Walker-Moran also highlighted the CREG's revisions for other major taxes: those on insurance premiums, liquor and personal income. The predicted effects of federal health care law implementation influenced revenue projections associated with the insurance premiums tax. The group predicts that liquor excise tax revenues will be steady but that recent legislative changes to related distribution schemes will decrease inflows to the GF by about $19 million during the years that the changes are in effect. It is expected that personal income tax (PIT) revenue for FY 2014 will be higher than had been forecasted in December.

Ms. Burrows Kleats resumed the presentation. FY 2015 estimated revenue is $56 million more than previously forecasted; the new revenue total represents 3.9% growth. In general, the national economy, as measured by employment, unemployment, the housing market, consumer confidence, interest rates and credit burdens, is improving. This optimism is tempered in part by federal fiscal austerity, the lack of spending growth and risks associated with interest rates and international trade. Ms. Burrows Kleats reviewed a graph showing the general improvement forecasted in statewide private and public employment and a table showing that New Mexico had 4,600 more jobs in August than in the previous August. She continued by saying that, at 41%, corporations in the service industry constitute the bulk of the GRT base. The most rapid growth of that base is associated with the mining industry and the manufacturing industry. Although down from a peak of 15% of the GRT base, there has been recent growth in the percentage of the base associated with the construction industry. New Mexico oil prices and gas prices increased in FY 2014, but they have dropped in recent months; the change will decrease revenue to the GF. Oil production has doubled since 2009, and growth, though at a slower rate, is expected. Meanwhile, gas production has stabilized and is expected to remain flat. Lastly, the total severance tax bond (STB) bonding capacity for FY 2015 is $577.3 million; $347.7 million of the total is designated for senior STB projects and $229.6 million for supplemental STB projects.

Mr. van Moorsel concluded the panel's formal presentation by discussing areas of uncertainty and risk that could significantly affect GF revenues and by elaborating on the GF balance. Notable areas of uncertainty include insurance premiums tax collection levels, earnings on state balances and tribal revenue-sharing. As factors affecting these issues become clearer, revenue estimates will be refined. Mr. van Moorsel noted that, because of uncertainty surrounding revenue associated with economic development-focused tax programs, the group uses a conservative approach to revenue estimation associated with them. He continued by mentioning the risks — both those posing favorable and those posing unfavorable potential consequences — surrounding: state and local government budget conditions; the economic recovery; federal reserve interest rates; federal health care reform; the Eunice lawsuit; the cost of tax credits; the tobacco settlement; the special education maintenance-of-effort issue; and a prior deficiency in Medicaid funding. Further, at about $670 million, or 11.3% of the budget for recurring appropriations, GF reserves exceed the LFC's target level of 10%.

On questioning, the panel elaborated on some of the risks it noted — citing, for some risks, the revenue figure associated with it. The panel and committee members discussed those and other topics as follows.

Risks and revenue estimates. Mr. van Moorsel indicated that the most recent revenue estimates reflect some of the identified risks, such as those related to tribal revenue sharing. Others, such as the Eunice lawsuit (aspects of which Secretary Padilla summarized) and changes in oil and gas prices, cannot yet be quantified and are not reflected in the group's calculations. Secretary Padilla stated that the TRD is calculating distributions to local governments as it did before the Eunice lawsuit. She suggested that it is unlikely that the proposed federal Marketplace Fairness Act, whose enactment would increase state revenue, will pass in the near future. Mr. van Moorsel reported that work on the state cash-reconciliation issue is still underway and that the high-wage jobs tax credit has been amended to align more closely with its intended purpose. Ms. Burrows Kleats said that oil is being produced at such a high rate that the main barrier to greater production is transportation. A committee member asserted that the state is overly reliant on the oil and gas industries for its revenue.

TRD administration. A member observed that much tax expertise at the TRD, considered essential to providing high-quality, accurate reporting, is lost to retirement and the private sector. Secretary Padilla attested that, in her tenure: (1) the TRD went from having vacancies in all but one economist position to having no vacancies in those positions; and (2) the department's rating by a national state tax organization improved. She described the TRD's efforts to attract and retain competent professionals, stressed the importance of investing in ongoing training and remarked that making the TRD's Protest Office independent of the TRD would further improve the TRD rating. She cited reasons that the TRD employs economists, which include that department employees have privileged access to information that influences revenue estimates.

Requests for more information. Ms. Burrows Kleats offered to supply more detailed data related to the pie charts on page five of her handout. Mr. van Moorsel agreed to supply the figure representing the FY 2014 deposit to the corpus of the Severance Tax Permanent Fund.

Annual Report — Locomotive Fuel GRT Deductions

Barbara Brazil, deputy secretary of economic development, and Ryan Gleason, director, tax policy and research, TRD, reported on the locomotive fuel GRT deductions.

Ms. Brazil began by providing some context for her portion of the presentation and an overview of the locomotive fuel deductions. By law, a legislative review of the deductions is required every six years beginning in 2019. The deductions were enacted in 2011 and amended in 2013. The 2013 amendment expanded the list of investment types that qualify a common carrier for the deduction. The Economic Development Department's role in the program is to certify qualifying taxpayers, promulgate rules for issuance of certificates of eligibility and track the number of jobs resulting from the incentive. Ms. Brazil reported that Union Pacific Railroad (UP) and the BNSF Railway Company (BNSF) have satisfied the investment requirements. She expounded on some of the companies' characteristics that relate to New Mexico and the deductions.

UP occupies a 2,200-acre site in the Santa Teresa industrial park and has invested more than $350 million in its facility. The facility's construction, which took place between mid-2011 and mid-2014, created 1,311 temporary jobs. It became fully operational in April 2014, and as of June 30, 2014, 406 permanent jobs have been created. Of those, 251 are UP employee jobs and 155 of them are contractor jobs. Ms. Brazil remarked on what she characterized as the region's explosive growth, in which UP played a key role.

Ms. Brazil next cited facts about BNSF's presence and investments in the state and noted that the BNSF fact sheet distributed to members contains recently updated information. BNSF recently increased its payroll and the number of its employees in the state. Its operating revenue increased from 2012 to 2013, and the company made capital improvements beyond what were required for the deduction. Ms. Brazil closed by saying that, as one of the largest private employers in Clovis and Belen and having a strong presence in Albuquerque and Gallup, BNSF also has the potential to develop in the state's southern region. A committee member commented that the fuel deductions have improved development in McKinley County.

Mr. Gleason followed with a report on the value of the locomotive fuel deductions. UP has deducted $9.8 million, and BNSF has deducted $5.3 million, from their respective GRT liabilities. Mr. Gleason stressed that the amounts represent high value to the companies but not lost revenue to the state. Were it not for the incentives, the companies would not have purchased — and therefore paid taxes on — fuel in New Mexico. Mr. Gleason continued by reporting that, based on data supplied by the Workforce Solutions Department and on certain assumptions, the TRD estimates that $1,578,706 was collected in PIT revenue during the three years of construction. He noted that GRT revenue generated by employee spending was not considered in the TRD's calculation of economic effect.

On questioning, Ms. Brazil, Mr. Gleason and committee members addressed the following topics.

Employees' state residence and New Mexico's economy. A committee member expressed the concern that if the companies' jobs are held by Texans, then most of the payroll is probably being spent in Texas and not generating GRT revenue. Mr. Gleason replied that including in the criteria for the deductions that employees be New Mexicans might not be feasible and that the transfer of some payroll spending to Texas is inevitable. Fred Ochesky, lobbyist, UP, who was in the audience, testified that seven out of every 10 UP subcontractors working on construction were based in New Mexico. Further, he said, although initially many employees commuted from El Paso, increasingly they are settling in New Mexico. Several members contributed their impressions and knowledge of the situation, including that: (1) part of the development strategy was to build affordable housing in the area in order to expand the New Mexico-taxpaying population base, but the 2008 economic downturn stymied that development; and (2) there is much two-way, cross-border spending, which produces an exchange between economies that can be considered healthy for the region.

Reporting on the deductions; GRT reform. A committee member requested more quantitative reporting on the deductions, which were acknowledged to have a generally positive net effect. Mr. Gleason indicated that the stated goal for the report to be delivered in 2019 is to have a refined understanding of the deductions' full fiscal effect, taking business development, payroll and housing development into account. Ms. Brazil added that the factors and data considered in the analysis are being determined. A member commented that in the effort to broaden the tax base as part of proposed GRT reform, incentives like the locomotive fuel deductions, which are clearly effective, should be preserved. To know which should be preserved, an effective method of measuring whether a given incentive yields such a gain is needed.

Update on Gaming Compacts with the Federal Government

George Rivera, governor of the Pueblo of Pojoaque, and Steffani Cochran, chief legal counsel, Pueblo of Pojoaque, summarized the status of the Pueblo of Pojoaque's efforts to enter into a new casino gaming compact with the state. The presenters provided a handout consisting of formal remarks outlining the pueblo's position on the matter and a handout with information about gaming industry trends, comparisons among states of their laws and gaming revenue and a comparison among New Mexico casinos of net-win figures.

Governor Rivera reported that, after attempting through nearly two years of negotiations with representatives of the New Mexico Office of the Governor for a new tribal-state gaming compact, the pueblo is pursuing an alternative course called secretarial procedures, in which the pueblo would work with the U.S. Department of the Interior to establish a new gaming compact. The pueblo's existing contract was entered into in 2001 and will expire in 2015. Meanwhile, the state has sued to challenge the lawfulness of, and prevent the pueblo from pursuing, the secretarial-procedures course.

Governor Rivera commented on: (1) the recent statewide and nationwide leveling and, in some cases, decline, in gaming revenue; (2) the challenges presented by market saturation; (3) the Pueblo of Pojoaque casino's contributions to the regional and state economies; and (4) the disagreement between the pueblo and the Gaming Control Board (GCB) on the correct tax treatment of free-play offerings, a question that was submitted to the state auditor for his review and response. Governor Rivera expressed his hope that the legislature or, perhaps, a new governor would consider the situation with the awareness that the pueblo is not an out-of-state corporation asking for a tax break, but rather a permanent in-state business that improves the state's economy and helps to pay for many public services.

On questioning, Governor Rivera, Ms. Cochran and committee members addressed the following topics.

State-tribal relations. A member expressed disappointment that the pueblo's negotiations with the New Mexico Office of the Governor failed and that the pueblo has had to resort to pursuing the secretarial-procedures course. The member remarked that the primary intent of the Indian Gaming Regulatory Act (IGRA) was to enrich economic development of the tribes, not the states. The member went on to question the propriety of the state deriving any revenue from Indian gaming and observed that the opportunity for the state to successfully negotiate with other tribes whose compacts will expire soon is diminishing.

Secretarial procedures and IGRA. Ms. Cochran indicated that one issue being addressed in the lawsuit is whether IGRA gives the U.S. secretary of the interior the authority to have established the secretarial procedures. Governor Rivera said that if the courts rule in favor of the state, the pueblo's next step would depend on the nature of the ruling. He added that the suit poses the risk that a court rules against the validity of all revenue sharing.

Gaming — Revenue, Trends and Tribal-State Revenue Sharing

Frank A. Baca, general counsel and acting executive director, GCB, reported on gaming trends and levels of historical and projected gaming-derived state revenue. After a period of flattening, there has been a slight increase in all gaming-derived revenue to the GF. Nevertheless, it is expected to decrease slightly from FY 2014 to FY 2015. The racetrack net take, or total amount wagered less jackpots paid, has vacillated since FY 2008 on a generally downward course. Tribal gaming revenue levels, meanwhile, have been edging up, but data suggest that they will decline slightly, with the market having reached a saturation point. Mr. Baca reviewed charts and tables showing: (1) the comparison among tribal net win, racetrack net take, racetrack taxes paid and revenue share paid; (2) the effect of gaming on horse racing; (3) the projection that revenue from nontribal gaming will remain approximately at its FY 2014 level; and (4) the projected estimates of FY 2015 gaming-derived revenue.

Mr. Baca also discussed the GCB's operations and budget. After a general decline, the GCB's budget recently increased. Mr. Baca reviewed charts showing: (1) the relationship between the operating budget and gaming revenue to the GF; (2) the number of inspections and citations in the past seven fiscal years; and (3) the level of activity by the GCB's Audit and Compliance Division. He noted that adequate staffing promotes compliance, and he reported that a statutorily required central system — which monitors nontribal gaming machines for tax and other regulatory purposes, and which, he said, promotes fairness and integrity — is installed and operating.

Mr. Baca closed by underscoring the saturation in the gaming market, a condition that tamps revenue growth. He noted that gaming establishments are proliferating on local, national and global levels and that other governments that collect revenue from gaming are similarly experiencing the effects of saturation.

On questioning, Mr. Baca and committee members addressed the following topics.

Tax treatment and accounting of free play. Mr. Baca acknowledged the dispute between the GCB and tribes over the tax treatment of free play and indicated that disputed amounts are not publicly disclosed because of confidentiality requirements. A member expressed dissatisfaction at that lack of transparency. Mr. Baca also explained that in Nevada courts, the issue of free play has been litigated and ruled on in favor of the state. Given that New Mexico's gaming regulations are similar to those in Nevada and other gaming states, there is support for the position that its regulation is appropriate.

Tax treatment of gaming establishments. A member pointed out, as a distinction between tribal gaming enterprises and racetracks, that tribes use gaming revenue for public works and services, unlike the private owners of racetracks; the member suggested that the distinction should be considered when developing related tax policy. Another member remarked that, in light of the recent trend to reduce the tax burden of businesses, tribal gaming enterprises are an anomaly. Mr. Baca responded that, historically, taxation of gaming served as a check on what was widely considered to be an immoral activity.

Santa Teresa's Industrial Border Zone

Jerry Pacheco, president, Global Perspectives Integrated, Inc., and vice president, Border Industrial Association, William Mattiace, executive director, Border Authority (BA), and Chuck McMahon, director, Planning Department, Dona Ana County, discussed the Santa Teresa-area border zone.

Mr. Pacheco explained causes of recent growth in the region. Many conditions affecting U.S.-Mexico trade have improved, and the Mexican economy is improving. Much of the expansion is attributed to Midwest companies moving closer to the border to tighten their supply chains. Exportation of products to Mexico from New Mexico has grown substantially; most of those products, which are intended for assembly in maquiladoras, originate in the Santa Teresa-Las Cruces corridor. Mr. Pacheco emphasized that these trends present an opportunity for New Mexico to continue to develop in its Mexican-border region.

Mr. Pacheco continued by describing development over the past two decades — and changes to law that he believes will promote continued development — in the Santa Teresa area. Previously, there was a high vacancy rate of commercial buildings; now, there is 99% occupancy accompanied by business expansion, state funding for water and wastewater projects, a solid business recruitment pipeline and a high job-growth rate. Notable companies in the region are Foxconn, a large computer-assembly plant that will soon move to San Jeronimo and take advantage of a new customs preclearance program, and UP. Mr. Pacheco proposed that, to foster continued development, the state: (1) appropriate money to improve the roads in the region; and (2) expand the overweight border commercial zone to encompass the UP intermodal facility.

Mr. Mattiace gave an overview of the BA vision, mission and organization and projects in which the BA is involved. Those projects include: (1) construction of a southbound road extending from Pete Domenici Highway to the border that would separate cars from commercial trucks to improve the flow of traffic; (2) a study to develop flood-control infrastructure in the Columbus area; (3) road improvements in Columbus; and (4) a $1.2 million rail feasibility study, for which the BA is the fiscal agent.

Mr. McMahon concluded the presentation by underscoring the tremendous development that has occurred in the region and the potential for development that still exists. He indicated that Dona Ana County is a grantee in the U.S. foreign trade-zone program, which encourages local economic development by relaxing duty requirements for foreign merchandise. Mr. McMahon reviewed the San Jeronimo/Santa Teresa master plan (noting the international importance of the region's development), limitations in the area's transportation network (noting the costs of some improvements, if undertaken) and some infrastructure improvements that have been made (noting that some housing and air-related developments are in progress).

On questioning, the panel and committee addressed the following topics.

Foreign driver's licenses. Mr. Mattiace offered to supply information about whether Mexican citizens' driver's licenses and insurance are valid outside of the border zone.

Regional growth and infrastructure. A member commented that a visit to the Santa Teresa region makes palpable the economic boom. The member expressed hope that growth is being controlled responsibly and that the challenges of paying for necessary infrastructure will be overcome. Mr. McMahon said that expanding the airport to increase personal aircraft activity and cargo activity would require infrastructure investments.

Approval of Minutes

On a motion made and seconded, the minutes from the August 5-6, 2014 RSTP meeting were unanimously approved.

The committee recessed at 4:20 p.m.

Tuesday, September 30

The committee reconvened at 9:00 a.m. for a tour of the UP facility, fueling facility and intermodal facility in Santa Teresa.